GERMANY'S REPARATION PAYMENTS

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The treaty of peace imposes upon Germany charges for reparations which cannot fail to entail far-reaching changes in the trade between her and other countries. Through a period of thirty years, more or less, she will be compelled to make heavy remittances to other countries. Without entering now on any close estimate of her obligations,—more will be said presently of the treaty clauses which define them,—it may be premised that they require the regular payment to the Allies of sums quite beyond anything heretofore known in international transactions on government account. The German Government will have to effect payments which can not be less than $750,000,000 a year and may reach, even exceed, a round billion.

The present paper is chiefly concerned with these huge foreign remittances and their consequences. The internal rearrangements which Germany may have to make are another matter. The German Government will have to find corresponding fiscal resources, through taxes and the like compulsory charges. This is a heavy burden, but not necessarily an impossible one. At all events, whatever the internal burden and the ways of carrying it, the problem taken up in the following pages is how a sum of this kind, secured by the German Government from its own citizens, can be remitted outside Germany, and what will be the consequences of the operations.

The orthodox or Ricardian theory of such a case can be easily worked out. In that theory, as the reader need hardly be reminded, it is assumed that specie (gold) is in use both in Germany and in the countries with which she trades. The order of events would be foreseen as follows. First, a rise of foreign exchange in Germany, due to the government's demand for bills wherewith to effect remittances to foreign countries. Pounds sterling, francs, dollars will be in demand. The specie export point will soon be reached and gold will flow out of Germany. Next, a period of lower prices in Germany and of prices continuing steadily to become lower. Conversely, there will be rising prices in foreign countries. Third, exports from Germany will increase, being stimulated by lower prices; imports into Germany will decline, being checked by that same situation. The gap between merchandise imports and exports will steadily increase, until finally that stage is reached when the total spread between the two will be

equal in money value to the sum total which the German Government needs annually to remit. Equilibrium will then be established. Merchandise exports from Germany will exceed merchandise imports by a billion a year (or whatever is the amount of the reparation remittances), and bills of exchange for that precise amount will be regularly at the disposal of the German Government. Specie will no longer flow; international trade will have adjusted itself to the new conditions.

When that stage has been reached Germany will be parting annually with goods valued at a billion dollars a year. These will go to the reparation countries and will constitute for them the real, the substantial reparation. They will not necessarily go to them directly. It is quite conceivable that Germany will send exports to third countries, perhaps South America, perhaps the Orient, perhaps Russia. From these goods will then flow to the reparation countries, substituted by an indirect process for Germany's own exports. Such cross trading and cross financing in international trade may be assumed to be familiar to the conversant reader. Whether from Germany or other countries, France and the others will receive goods, wares, and merchandise, and Germany will send out an equivalent amount of her own annual product.

What is less familiar, and may be dwelt on for a moment, is that Germany sustains a further loss than that measured by the billion dollars. Her people will have, throughout the period over which the reparation payments are spread, money incomes which are lower. Conversely, other countries and especially the reparation countries will have money incomes which are higher. Germany not only parts with exported goods, but parts with physical quantities of those goods greater than she would have had to part with at the scale of prices and incomes that prevailed before the operation set in. Germany delivers more of exported goods than would have sufficed to make up a billion dollars during the preceding period. Moreover, the imports which she continues to buy are less in quantity than before, not only because she receives less money's worth, but because the imports, less than before in terms of money, are even more diminished in terms of physical quantity. This loss is more obscure, less likely to be perceived or consciously felt, than the overt remittance, but is none the less real. It is the inevitable consequence of the process by which the direct reparation payments have to be effected,—a process in the course of which Germany must induce other peoples to take more and more of her exported goods, and must herself take less and less of im-

ported goods, in order to make up the needful sum total of money remittances.

Push this reasoning a stage further. Sooner or later, say in a generation, the transaction will be finally wound up. The reparation payments will cease. What then?

Obviously there will be radical readjustments; indeed, complete reversal. The German Government will cease to be in the market for bills of exchange. German exporting industries none the less will still be producing; and they will continue to produce for export and to send out their goods so long as foreign markets and foreign prices remain what they had come to be during the preceding period. As the exports continue, however, and now exceed not only the imports but the sum total of Germany's debit obligations, specie will flow back to Germany. Prices and money incomes will rise in Germany. The exporting industries will go through a period of poor business and depression, and exports will gradually be checked. Imports on the other hand will be tempted. A continuance of these operations, of which the one is of course the obverse of the other, will lead finally to a stage of equilibrium identical with that which prevailed at the very start. With the increase of imports and decrease of exports, a normal merchandise balance will again be reached. Prices will have risen in Germany, presumably to their previous level; prices in foreign countries will have fallen, presumably to their previous level.

On this point—the eventual backflow—I take it on me to digress for a moment. The backflow is the consequence purely and simply of the cessation of the reparation remittances. It is a common error to suppose that shifts in international trade of this and similar character lead to a backflow under any circumstances,—to a reaction during their very course. It is supposed that during the course of *any* remittances the flow of specie from one country to another necessarily counteracts itself, leading to a return of the specie which had begun to move. This is quite erroneous. If there be a continuing and unceasing remittance, for example a perpetual tribute, specie will flow out of the tributary country and into the receiving country until the readjustment of imports and exports supplies a merchandise balance equal to the tribute. Then the flow of specie will definitively cease. No backflow will ensue. There will be permanently higher money incomes and prices in the receiving country, permanently lower prices in the paying country. So it is, in the strict theory of the case, whenever remittances have to be made unceasingly on other than merchandise account. The occasion for the remittances may be tourist expenses,

interest dues, ocean freights, or what not. So long as they continue, they lead to a sustained readjustment of international prices and incomes, initiated by a flow of specie. There ensues a redistribution of the specie supply among the countries concerned, not counteracted by a backflow but maintained without disturbance so long as the remittances themselves continue.

The characteristic of a reparation or indemnity charge, however, is that by its terms it does *not* go on indefinitely. It comes to an end once for all at a predetermined date. Then, and then only, readjustment and backflow set in. In other transactions,—tourist expenses, for example,—the need for remittance goes on indefinitely; in still others, such as lending and borrowing transactions with their accumulating interest accounts, there may be shifts, gradual or abrupt. Whatever the impelling force, so long as it continues, there will ensue an equilibrium adapted to the modified conditions, a sustained change in the international distribution of specie, and corresponding sustained changes in the price levels of the several countries.

To return now to the analysis of the earlier stage, during which no backflow can be deemed possible. Unfortunately there is nothing in economic experience which is of service for verification or revision of the theoretical conclusions. The indemnity remittances required in the past from countries of less advanced civilization, such as Turkey and China, have taken place under so many complicating conditions as to be of little pertinence. The only large operation of the kind between great civilized countries is the Franco-German indemnity following the war of 1871. Yet this also serves little for the present purpose. In the first place one lump sum was paid, the famous five billions of francs,—paid in a very short stretch of time. In the second place, the payment was effected by a process which could avail only for an operation to be wound up in a brief period. France achieved the task in the main by utilizing the foreign securities then held by her people, constituting potential assets distributed widely over the world. A single great payment can be effected in this way, and was so effected. Something of the same sort was done (spread over a period a little longer) when, under different circumstances and with a different object, Great Britain and France paid the United States for our extraordinary exports of 1916-17. No such process can be made available for heavy remittances continued at a regular rate over a long period, such as Germany has to provide for.

But quite apart from any qualifications or corrections which past experience might suggest, the international payments called for by

the reparation requirements are so huge in volume, so vastly greater than had ever been imagined, that the theory of the case, as set forth above, must be revised and modified. Two things stand out as inevitable. First, the ordinary mechanism of international trade,—specie outflow, price changes, and consequent changes in exports or imports,—cannot cope with transactions so huge. Second, whatever the mechanism that may serve to bring about the eventual outcome, that outcome can be nothing else than a great and constant excess of merchandise exports from Germany. These two aspects of the problem I will take up in order.

I

Even if the case were of the simplest sort,—if both Germany and the reparation countries were on a specie basis,—no outflow of gold from Germany can be conceived which would bring about a fulfillment of the enormous requirements. If the German Government were to undertake remittance by purchasing bills of exchange in the market, then allowing specie outflow to set in and to last until automatically brought to a close, Germany's circulating medium would be completely drained in a few months, at most in a year. Exports and imports of merchandise could not possibly accommodate themselves in short order to such overwhelming changes. One might indeed indulge in the intellectual exercise of imagining the problem to work itself out to the bitter end. It could be doubtless argued that eventually there must come a readjustment in accord with the fundamentals of theory. But such drastic adjustment could be reached only after a period of monetary revolution and credit collapse which would affect not Germany alone, but the entire world. It would be idle to speculate on possibilities of this sort.

The reparation clauses and the remittances called for by them may now be considered somewhat more in detail, that we may get nearer to the probabilities or possibilities of the case. The treaty provisions on this subject divide themselves into three parts. In the first place Germany is to pay five billions of dollars by May 1, 1921.[1] This first block payment, however, will virtually not figure in the remittance operations. As credits toward making it up, Germany is to be allowed to count all the ships, securities, coal, machinery, cattle, and like immediate assets which she may turn over to the Allies until the date mentioned. Whatever remains to be paid after these credit items have

[1] For simplicity, I reckon the gold mark as equal to a quarter of a dollar,—20 billion marks equal to 5 billion dollars.

been exhausted is to be charged with no interest, but is to be converted on May 1, 1921, into interest-bearing bonds of the character described under the second head. It is impossible to say how much the credits will amount to and how much will remain to be funded into the interest bearing bonds. I should suppose that a very liberal estimate would be to allow one half of the total (two and one half billions) on account of the credit items, leaving the same amount to be funded in 1921.

Second, Germany is to issue at once ten billions dollars of bonds, which are to bear interest at 2½ per cent between 1921 and 1926, and after 1926 5 per cent with an additional 1 per cent for amortization. To this sum of ten billions must be added in 1921 the unpaid obligations under the first head, which, as has just been noted, can hardly amount to less than two and one half billions. The minimum of the principal of the bonds will then be twelve and one half billions. The interest charge on twelve and one half billions at 2½ per cent would be $312,500,000 for 1921-26, and after 1926, when the interest charges will be at the full 6 per cent, $750,000,000 a year. If the unpaid obligation under the first head is more than two and a half billions, as is probable enough, the interest charge will be so much higher.

Third, there is an indeterminate obligation,—a possible ten billions of dollars more,—to be issued "when and not until the Reparation Commission is satisfied that Germany can meet the interest and sinking fund obligations." How much more will be added on this score to the total interest charge,—that is, to the total remittances which Germany must make,—it would be rash to estimate. I should be surprised if the Reparation Commission should find Germany able to meet obligations in excess of a billion a year; even that sum is a high maximum.

A considerable period of transition is thus provided for, during which Germany may prepare to pay and the Allies themselves may prepare to receive. Considerable changes may take place in the intervening period and not a few difficulties may be obviated by foresight and preparation. But when all is said, a new factor of enormous importance will within a few years influence the international trade of all civilized countries. Germany will have to remit a billion a year, more or less, to foreign parts. How can it be accomplished?

All this, as has been sufficiently indicated, would introduce complications enough if the countries concerned were on a specie basis. In fact, however, most of the Allies are not now on a specie basis. Germany herself is most deeply in the throes of a paper money regime.

The chance of her escaping from it at an early date is slender indeed. For a considerable time, she will have paper prices, no gold points, no specie to flow out of her circulating medium, foreign exchange reckoned in depreciated paper. Under such anomalous conditions how manage such anomalous transactions?

This harks back to an old problem. What, under a paper regime, is the relation between the rates of foreign exchange, the specie premium, and the "real depreciation" of the paper (the general level of prices)? Ricardo and his followers assumed that all three,—foreign exchange, specie premium, and price level,—moved together in precise accord. They not only so assumed, but probably believed that their assumption was in accord with the facts. And it is true that two of the phenomena are thus in harmony: foreign exchange and the specie premium do run together. Experience shows abundantly, however, that the real depreciation of the paper, the general level of prices, may diverge widely from the other two. The divergence is specially wide and specially prolonged for domestic commodities,—such as are bought and sold solely within a country. It is less so for the international goods, which are the objects of export and import trade; yet it is considerable and lasts long for the international goods also. Not only are there such divergencies, but they are connected with international trade and with the rates of foreign exchange both as causes and as effects. There are reflex and interacting phenomena of the most perplexing character.

Assuming now that Germany remains on a paper money basis, what rates of foreign exchange are to be expected? It is obvious that there will be a steady and insistent demand by the government, month by month and year by year, for bills on London, Paris, New York, Amsterdam, Madrid, Copenhagen,—anything that will serve for remittance. That demand will tend steadily to raise in Germany the price of exchange on foreign countries and to depress in foreign countries exchange on Germany. And in consequence there will be a tendency for the price of foreign exchange in Germany to be kept *higher* than would accord with the course of commodity prices. For a long time there will be a divergence between the general price level and the rates of foreign exchange. The divergence means that exporters will be in a position to profit. They can buy cheap (comparatively cheap) in Germany, sell the German goods abroad, draw on the foreign purchasers and sell their exchange to advantage at home. Quite the reverse will be the situation of importers. They will not

be able to sell to advantage in Germany and will have to pay high for the means of remittance to the foreign vendors. The whole situation obviously will tend to attract labor and capital to the German exporting industries and to repel them from the importing industries. The greater the divergence between foreign exchange and the commodity price level, the more rapid and extensive will be these transpositions of German industry.

The process means simply that a given amount of German labor and capital is turned to the specific object of reparation. The exporting industries provide goods which go to foreign countries. No imports arrive in return. Identically the same thing happens, only through a different mechanism, as that which is provided for in the treaty clauses which require Germany to send to France, Belgium, and Italy so many tons of coal, so many head of cattle, so much railway material and agricultural machinery.

Observe, however, that the process is not so consciously directed to its purpose. It is true that some deliberate utilization of this peculiar state of foreign exchanges may be made by the German Government. But I suspect that in the main there will be simply the prime and conspicuous force of an unceasing demand for foreign exchange,—no intention that thereby pressure will be directed toward pushing exported goods out of the country. And under a specie regime also, the outflow of goods which ensues is the undesigned consequence of the remittances to foreign countries, taking place without deliberate intent on the part of the government or of the trading community.

Under a paper money regime, however, the mechanism is not only different in character, but probably of greater efficacy. A paper money regime and the great and rapid shifts in foreign exchange which it renders possible will apparently exercise pressure on the movement of goods more rapidly than would the same operations under a gold regime. It promises to play into Germany's hands in an unexpected way. The shift to new conditions of international trade and to new relations between exports and imports, and the procurement of the great quantity of foreign exchange, are likely to be most difficult during the very first years. Once the transition is over and the new state of equilibrium reached, things will go more smoothly. And apparently that smooth and comparatively stable situation will be reached more quickly, more automatically, because of the very circumstance which ordinarily would be a disturbing and dangerous factor in international trade,—a depreciated paper money regime.

The divergence between foreign exchange and the general level of prices, considerable and striking as it may be in the early stages of this curious transition, will tend to decrease as the transition is completed. The drift of labor and capital to exporting industries and the increasing supply of exported goods will tend to bring out larger and larger amounts of foreign exchange and so to lessen the premium on exchange in Germany. The decline in imports will work in the same direction. German prices and German incomes, both in exporting and in importing industries, will gradually accommodate themselves to the new situation. Foreign exchange, specie premium, and the general level of prices, will finally tend to come together. The kind of parallelism between foreign exchange and domestic prices which was assumed in Ricardian theory will emerge in the end.

II

So much as to the first of the outstanding features of the case: the mere mechanism of payment. Turn now to the second: the concrete form in which the payments must be effected.

There is but one possibility. The substance of the payments will be in goods and in goods only. Germany can remit only by sending out merchandise, and the limit of remittance is found in the possible excess of merchandise exports over merchandise imports. The extent of reparation that can be secured is limited by the available amount of exportable goods.

In many estimates and speculations concerning the maximum which Germany can be made to pay, figures have been put together showing her total wealth and total resources. All such calculations are quite beside the case. Statistics of wealth, property, total possessions, have nothing to do with reparation possibilities. That part only of her property and wealth can be looked to for reparation purposes which can be delivered to the Allies and used by them. Her fixed wealth in the form of lands, houses, railroads, factories, is quite unavailable (subject to an exception, not important, presently to be mentioned). Nothing in the way of plant can be moved away or put at the disposal of foreigners. The one and only way in which payments can be made to foreigners is by turning over to them things which they can take and will take. These things include on the one hand such easily movable assets as gold and securities; but, as already indicated, everything of this kind will have been exhausted before the sustained flow of reparation payments sets in. They include also the exportable goods, wares, and merchandise; and here are the specific assets which alone remain

for utilization. If a capital sum is to be fixed,—a total representing the present value of a series of payments spread over many years,—that sum is simply the capitalized value of the maximum excess of Germany's merchandise exports over her merchandise imports. Somehow a huge favorable balance of trade (never has the phrase had greater irony) must be rapidly developed. Exports must expand, imports must shrink. By this process, and by this process only, can the wherewithal be provided for sending to other countries what is due on reparation account.

Before proceeding to the corollaries that flow from this proposition, let us note the one qualification to be attached to it. There is a conceivable way in which lands, houses, and railroads in Germany could be used for reparation purposes: namely, that foreign investors should buy this irremovable property, and arrange to pay the purchase price to the reparation countries. In view of the extreme difficulty of handling investments thus left in Germany; in view of the drain impending in any event upon the available savings of foreign countries; in view too of the extreme reluctance of the German Government and the German people thus to part with the command of their own industrial outfit,—this possibility seems to me almost negligible. Moreover, it would promptly lead, as the conversant reader needs hardly be informed, to a need of further remittances out of Germany. The interest and profits on these investments by foreigners in Germany would have to be sent, and for these again the only resource would be merchandise exports. There is here no serious qualification of the main proposition. To repeat, the only way in which Germany can meet her obligations is by an excess of merchandise exports equal in value to the interest and amortization of the reparation bonds; that is, not far from a billion dollars a year.

Such being the situation, the German Government must consciously and deliberately grapple with the task. No country, Germany least of all, would rely solely on automatic trade adjustments for the procurement of this enormous supply of foreign exchange. There must be search for ways of deliberately stimulating exports and deliberately checking imports.

Import restrictions are an obvious device. They have been utilized in Great Britain and France and other European countries during the war for essentially the same reason, namely, that the ordinary mechanism of foreign trade did not bring about that diminution in the purchase of foreign goods which was deemed necessary in the public interest.

Germany may be expected to prohibit some imports and to impose high duties upon others. Import restrictions doubtless will in part be sumptuary in character, designed to lessen the consumption of articles of luxury, even of comfort. It is quite within the bounds of possibility that they will also have a slant in the direction of protection. Such combination of fiscal and protectionist policies is familiar enough.

But restriction of imports will not alone suffice. Exports must be enlarged as well as imports lessened. The circumstance that German imports consist in large part of raw materials or indispensable food supplies puts a limit on the effective application of import restrictions. But devices for promoting exports may be expected to be utilized to the limit. And their utmost utilization can not be consistently objected to by the reparation countries. Among those available are export bounties, special rates of transportation for exported goods, and specially reduced prices of export commodities. Remission of taxes or reduction of taxes on exporting industries might also be on the list. Under ordinary circumstances practices of this sort are to be condemned in the interest of the very country that applies them.[2] Though they may promote export trade, they do so to the disadvantage of the exporting country itself. Their advocacy and defense usually rest upon a crass mercantilism. But in a case like the present all the usual reasoning ceases to apply and the ordinary objections cease to have weight. When it comes to the tremendous task of financing these reparation dues, any and every device for promoting exports would seem to be in order. They may mean a loss to the exporting country; but Germany as an exporting country obviously is doomed to incur a loss. She is under the necessity of turning to any and every method of meeting the necessities of the case.

Consider now, however, another consequence. Suppose Germany does promote exports in every possible way. What sound and fury there will be from the protectionists and mercantilists of other countries! Here is Germany the vanquished, the necessitous, the country compelled to disgorge,—entering on the very career of a "war after the war" which these same protectionists and mercantilists had most feared and reprobated. She prohibits imports or imposes high duties. So far from constituting a docile market to which the conquerors can ship goods without let or hindrance, she arrogantly refuses admission to their wares. And as regards exports, here is penetration with a

[2] I have considered the working of such practices, under normal circumstances, in my volume *Free Trade, the Tariff and Reciprocity,* chapter V.

vengeance. A sinister Germany emerges, bent upon trade conquest. The very steps for forcing export trade which have been so often placarded before an abhorrent world as deeds of the arch criminal are now resorted to more deliberately and upon a greater scale than ever before.

Not only will there be horror and wrath among the true blue protectionists in countries hostile to Germany, but the gentry of this same type in the Fatherland will rejoice. They will find in the achievement of a *Weltmarkt* some compensations for their humiliation. Germany's exports will be permeating the world and bringing countries near and distant "within the sphere of her influence." Notwithstanding the plain fact that these exports, being so much tribute, yield nothing at all to the country, the mercantilist attitude will infallibly persist. It colors so indelibly the thinking of the ordinary man and the everyday financial writer that it may persist even in the face of this *reductio ad absurdum*. Germany is selling, selling, selling; and is not this the way in which nations always get rich? True, the sales serve merely to enable the country to meet the obligations of defeat. None the less, they will be deemed by those astute folk evidences of commercial victory.

Further, it is obvious that there is much in the deliberate plans and expectations of the Allies which runs entirely counter to this sort of commercial change. Their own trade programs are flatly inconsistent with the program which through the reparation requirements they impose on Germany. They have been solicitous to promote their own export trade and to supplant Germany in every foreign market. The English have ousted the Germans in every cranny throughout the Orient, South America, Africa, the Levant. French and Italians are no less bent on the same end. Germany's colonies are gone. Whatever open door principle may be accepted for colonies under the mandatory system, it is tolerably certain that every mandatory power will find ways of making the market most open for its own goods. Germany's ships are gone too, at least for many years to come. True, there is exaggeration in the current talk about the necessity of a merchant marine of a country's own for the purpose of enabling it to carry on an export trade. Export trade can be developed without ships, as is amply proved by the pre-war experience of the United States; even foreign ships, when they bring imports into Germany, must plan to secure freights out of Germany also. But some interrelation doubtless there is; your own ships may be made to aid as instruments for promoting your own trade; and the absence of a merchant marine will

constitute a handicap upon the development of Germany's export trade. And yet,—it is so obvious as to seem wearisome, although persistently overlooked in most public talk,—it is only by exporting that Germany can make reparation. The Allied countries, so far as they smother Germany's exports, as they persistently are trying to do, are cutting off the nose to spite the face.

Whither now will Germany export? In part no doubt directly to the reparation countries and to the other Allies; in part to third countries, which in turn will send commodities to reparation countries.

All protectionists, especially in the Allied countries, most of all in the reparation countries, will furiously oppose direct exports into their own domains. Everything points to a maintenance, even to a strengthening, of the protectionist attitude in France and Italy. Exports from Germany to those countries will long be resented. England has always been a better customer for Germany than the others, and may continue to be a good customer. No one can foretell what will be the commercial policy of England after the first burst of passion has run its course. And who can say whether the United States tariff system will be relaxed? Moreover, the protectionist feeling has been so intensified by the hatred engendered during the war that tariff duties on imports from Germany are likely to be reinforced by boycotting. At the very best the direct exports from Germany to the Allies may hold their own; they will hardly be allowed to increase.

Elsewhere too the possibilities are dubious, in view of the attitude of the Allies as described in the preceding paragraphs. No German colonies remain. This market was at no time a large one,—the Germans themselves exaggerated its importance,—but such as it was and is, what between chicanery and the natural influence of political preponderance, the lion's share will fall to their rivals. A somewhat similar situation must be contemplated, at least for many years to come, in South America and the Orient. All the Allies, and particularly the British, will try to reap the fruits of the policy which they followed during the war,—ousting German firms and banks, and cutting out all German connections, with the express object of securing the trade which Germany had built up.

The one direction in which a considerable expansion of German trade may be looked for is in Eastern Europe and especially Russia. Here the possibilities are considerable. Not only are they considerable, but they are to be welcomed. On all but bald chauvinistic and mercantilist grounds the development of Russia by Germany is to the advantage of both countries and to that of all the world. And everything in

the political and social situation of the two peoples points to the probability of their eventual economic coöperation. The ulterior political and social consequences no one can predict. The experiments in a reconstruction of society of which they are likely to be the scene during the coming generation will be among the most instructive and indeed fascinating that have ever come under the observation of the economist. Whatever their course and outcome, they seem likely to be accompanied by trade developments in which Germany will supply manufactured goods to Russia and Russia will make payments in large measure through the export of food and raw materials. And here, to repeat, is a source from which Germany may procure the wherewithal for her reparation payments.

Such are the various possibilities and probabilities. How are they to be assessed by the cool headed? What is there of real good and real ill to Germany and the Allies?

The processes just described are, to repeat, those by which the reparation countries *get* what they are awarded. Germany receives nothing for the exports which she sends to the various markets. Directly or indirectly goods reach France (that country may be taken as the outstanding and typical reparation country) and thereby France secures the substance of reparation. She gets it in the only concrete form in which it can possibly do her good,—in things to eat, wear, use, and enjoy.

We may brush aside notions that all this is a cause of loss to France, not of gain. Advocates of peace have been disposed to urge that militarist exactions cannot under any circumstances be of real advantage to the victors themselves. The effects of the Franco-German indemnity of 1871 have been adduced as a warning example. Doubtless that indemnity was not an unmixed boon to the Germans; but none the less it was a clear source of material gain to them, promoting in no small measure the first steps in Germany's remarkable industrial development. France, too, will gain from her reparations; she will at least be better off with them than she would have been without them. She will secure tangible economic gain.

And yet France (to use that country still as typical) must face the fact that the gain will not be secured without some disturbance of existing conditions and without some possibilities of unwelcome concomitants. Goods come from Germany gratis. They may be dubbed reparations,—not gifts, but mere replacement of what was destroyed or taken; yet for the moment they are virtually the same as gifts. The

goods so supplied take the place of similar goods which might have been secured in other ways, perhaps are being secured at the very time in other ways. At least the possibility of changes and readjustments in France herself must be faced.

Two kinds of cases may arise, corresponding to the two forms which Germany's export trade may assume. There may be direct export of goods from Germany to France, as of coal, iron, woolens. The labor and capital which formerly produced these same things in France will be free to turn to something else, perhaps *must* turn to something else. Indeed France must somehow direct a part of her productive forces to the actual work of reparation,—to rebuilding villages, factories, railways. Needless to say the protectionists will endeavor with all their might to prevent the diversion to this task of forces now engaged in familiar industries. Thus, the treaty of peace prescribes specifically that Germany must deliver to France quantities of coal, cattle, machinery, materials, furniture. Yet if these same things should be *sold* by German exporters for delivery in France, there will infallibly be resentment. Obviously either method means that labor and capital which might have turned to these same things in France become free to do something else.

Second, there is the indirect process. Germany, for example, exports to Russia and Russia sends flax, wool, timber to France. If this takes place, France in turn cannot export to Russia as much as she might if Germany were out of the way. The expansion of her exports meets with a competition which will be arraigned as illegitimate, if not wicked,—the competition of a country which has not only low and declining money costs (wages and prices) but which is deliberately developing exports in every possible direction by every possible means. So with England. Germany will "invade" markets coveted by England and will rouse the ire of the British traders.

In sum, the reparation countries cannot get the substance of what they have insisted on without disturbance and readjustment in their own industrial organizatlon. It is indeed conceivable, though highly improbable, that all the imports into (say) France which the reparation payments will bring about shall take the form exclusively of food and raw materials not produced within her limits at all, or so produced that the imports will always supplement the domestic supply, never displace any part of it. Even so, some disturbance of existing conditions seems inevitable throughout the countries and the branches of trade coming within the scope of these extraordinary operations. Imports and exports will shift as trade balances and international

price relations come to be readjusted, and the several countries and the several industries within them must in some measure submit to corresponding modifications.

There is more. Eventually the wind-up of the whole reparation business will come; and then a second series of readjustments must ensue, in the opposite direction. A return must take place to international and domestic trade in which reparation payments no longer play a part. The pains of transition will have to be suffered twice: first while the economic world adjusts itself to the process by which reparation is accomplished, and again when the cessation of this process compels a return to the old and more normal state of things. The problems are similar to those which played so large a part in the former German debate between the advocates of *Agrarpolitik* and *Industriepolitik*. In that controversy, it will be recalled, the advocates of *Agrarpolitik* maintained that unrestricted manufacturing development meant a great diversion of labor and capital to manufacturing industries, followed after a generation or generations by an inevitable reversion to the old conditions and a return to a self-sufficing *Agrarstaat*. Even if willing to admit gains from the initial growth of manufacturers, they urged that the gains were more than offset by the losses from the double transition. The balance of gain and loss was not easy to calculate, and very likely was the other way; yet a question of offsets did arise. So in the present case: there will have to be a double set of adjustments, one at the beginning of the process, another at its end. The lost motion necessarily arising from shift and change is an offset to the tangible material advantages secured by the reparation countries during the period of reparation itself.

To all this may be added a word of warning,—which in the utterances of the fervid foreign trade promoters would become a prediction of disaster,—on the future export trade of European countries. Some real basis there may be for the forebodings of our friends the mercantilists. It must be admitted that the countries of Western Europe are under a virtual necessity to maintain and even to increase exports, in order to secure the wherewithal to pay for the food and raw materials which they must have. Their needs for these things vary in degree; France perhaps is least necessitous, England most so; but all are in essentially the same case, and all must count on maintaining an export trade. In such trade, it must further be admitted, established position, connection, prestige, habit, custom count heavily. Such factors tell in disposing of goods under any conditions, and tell perhaps most of all in selling for export. Germany will have been compelled

during the reparation period to develop by main force a great export business. When the end of the period comes, there will no more be an automatic cessation of her exports than at the beginning there was an automatic start of those exports. She will be in possession of an export market which, however distributed geographically, will be well established. Having developed it, she will be in better position to hold it.

A word of caution as I conclude. I have spoken about the future in terms not sufficiently guarded. Much of what has preceded is matter of speculation; and it might have been wiser to give warning at every stage how cautious one must be in venturing on prediction. We are still some way from 1921, and a long way from 1926; and not until 1926 are the reparation provisions planned to be in full effect. Many things may happen before that time, in the political field as well as in the economic. The reparation program as it stands in the Treaty may be much altered, perhaps quite upset. It remains to be seen how far the conditions assumed in the present analysis of the case will prove to obtain. My forecast must be understood to be of a hypothetical nature. Only if the assumed premises hold good, is it to be expected that the consequences will ensue as predicted.

One remark may be made about the chances of the fulfillment of the reparation program. France and the other Allies need disposable means at once,—ready funds. They must market the German bonds; or else their own securities based on the bonds, presumably with some sort of endorsement or guarantee. But market them they must in order to command the resources they need at this very moment. Once they have put the securities in the hands of investors, they have given hostages to fortune. Thereafter they *must* permit, nay facilitate, German arrangements for export. A distinguished French statesman—one whose name, were I free to give it, would carry weight—remarked to me, in the course of a conversation in which the inevitableness of Germany's expanding exports was pointed out: "if this proves to be the case, if Germany cannot pay without competing with us and displacing us in the export trade of Russia and Siberia,—we will simply cancel the reparations." The answer is that when once the Allies have cashed in the German reparations by selling the securities to investors, no cancellation is possible. Either they must refrain from the initial commitment or else they must allow the contract to be carried out to the bitter end.

And so, like all the international arrangements that the war has led to, this one faces a problematic future. Who can say what sort of world we shall find ourselves in ten years hence?